# (19,307.)

# SUPREME COURT OF THE UNITED STATES.

## OCTOBER TERM, 1904.

## No. 232.

WESTERN TIE AND TIMBER COMPANY, APPELLANT,

*vs.*

BEN A. BROWN, TRUSTEE OF THE ESTATE OF S. F. HARRISON, A BANKRUPT.

APPEAL FROM THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE EIGHTH CIRCUIT.

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JUDD & DETWEILER, PRINTERS, WASHINGTON, D. C., JUNE 14, 1904.

1 Pleas and proceedings in the United States circuit court of appeals for the eighth circuit at a term thereof begun and held at the United States court house in the city of St. Louis, Missouri, on the first Monday in December, being the seventh day of December, A. D. 1903, before the Honorable Walter H. Sanborn, Honorable Amos M. Thayer and Honorable William C. Hook, circuit judges.

Attest:

[Seal United States Circuit Court of Appeals, Eighth Circuit,]

JOHN D. JORDAN,
*Clerk of the United States Circuit Court of Appeals for the Eighth Circuit.*

Be it remembered that heretofore, to-wit: on the eighteenth day of July, A. D. 1903, a transcript of record, pursuant to an appeal from the district court of the United States for the eastern district of Arkansas, was filed in the office of the clerk of the United States circuit court of appeals for the eighth circuit in a certain cause wherein The Western Tie and Timber Company is appellant and Ben A. Brown, trustee of the estate of S. F. Harrison, bankrupt, is appellee, No. 1953, and that in pursuance of general order number 36 of the general orders in bankruptcy relating to appeals, the following portions of said transcript are certified in accordance with the præcipe of counsel for the appellant, Western Tie and Timber Company.

(*Order of Reference.*)

In the Matter of S. FRANK HARRISON, Bankrupt. No. 48.

Whereas on the 24th day of February, 1903, a petition was filed to have S. Frank Harrison, of Pocahontas, in the county of Randolph, and district aforesaid, adjudged a bankrupt, under
2 the acts of Congress relating to bankruptcy, and whereas the judge of said court was absent from said division of said district at the time of filing said petition, it is thereupon ordered that said matter be referred to Charles F. Cole, one of the referees in bankrupty of this court to consider said petition and take such proceedings therein as are required by said acts, and that said S. Frank Harrison shall attend before said referee on the 6th day of March, 1903, at Pocahontas.

(*Order of Adjudication.*)

In the District Court of the United States for the Northern Division of the Eastern District of Arkansas.

In the Matter of S. FRANK HARRISON, Bankrupt.

At Batesville, in said district, on the 24th day of February, 1903.

On this day received from J. W. Parse, clerk of this court, certificate of the absence of the district judge from the said division, and an order of reference with the petition and schedules in the matter of S. Frank Harrison, of Pocahontas, in said district, in bankruptcy.

And upon due consideration of said petition it is ordered that the said S. Frank Harrison be, and he is hereby adjudged and declared to be a bankrupt within the true intent and meaning of the acts of Congress relating to bankruptcy.

CHARLES F. COLE, *Referee.*

(*Proof of Claim of Western Tie and Timber Company.*)

In the District Court of the United States for the Eastern District of Arkansas, Northern Division.

*In re* S. F. HARRISON, Bankrupt. No. —. In Bankruptcy.

On this fourteenth day of May, A. D. 1903, comes Walter Poleman, and upon his oath says that he is the treasurer of the Western Tie and Timber Company, a corporation under the laws of
3 the State of Arkansas, and that S. F. Harrison, the person by whom the petition for adjudication of bankruptcy has been filed, was, at and before the filing of said petition, and still is justly and truly indebted to said corporation in the sum of $22,154.26, evidenced by his promissory note executed to the said corporation on the 16th day of January, 1903, the original of which was exhibited to this court heretofore by said Western Tie & Timber Company, and a copy of which is now on file with the court in proof of indebtedness heretofore filed by said Western Tie & Timber Company, against said bankrupt, and a further copy whereof is hereto attached. That the consideration of said note is money loaned and advanced by said Western Tie & Timber Company to said bankrupt, and that there are no payments on the same, and no set-offs or counter-claims against the same, except as may otherwise in this proof appear.

And that neither the Western Tie & Timber Company, nor any person or persons by its order, has or holds any sort or character of security for said claim other than herein set forth.

And affiant further says that on said 16th day of January, 1903, the said bankrupt was indebted to the said Western Tie and Timber Company, in addition to the amount of the said note, in the sum of $5,570.00 for money loaned by the said Western Tie & Timber Company to said bankrupt, and for which additional sum of money no note was had, or has, been taken, and that on said date the total amount due by said bankrupt to the Western Tie & Timber Company for money so loaned and advanced, was the sum of $27,724.26, and that on said date the Western Tie & Timber Company took possession of certain chattel property upon which it had been previously given a mortgage by said bankrupt as security for said debt, and agreed with the bankrupt upon the sum of $5,570.00 as the fair value thereof, and having given the bankrupt credit for that amount on account of said indebtedness, took his note for the balance due, being the note heretofore proved and herein again proved against said estate.

4 And the said affiant further says that since that time, it has been adjudicated by this court that said Western Tie & Timber Company was not entitled to any of said property under said mortgage other than that set out in the annexed account, and he further says that the value of the property as credited to said debt in the annexed statement is at least equal to the full, fair cash value thereof and to the value thereof in the appraisement herein as far as it has been appraised and that the only security held by said Western Tie & Timber Company for either of said claims is the total value of said property held under said mortgage as set forth in the annexed account, to-wit: the sum of $2,309.00.

And he further says that there have been no payments thereon, and that there are no off-sets nor counter-claims thereto other than such as are shown on the annexed account amounting, in the aggregate, to the sum of $1,167.96. And that the total sum now due the said Western Tie & Timber Company is the amount of said note with interest, and said sum of $5,570.00, less $1,167.96, off-sets, and $2,309.00, as the total value of the property held as security, leaving a net balance on said account of $2,093.04 due said Western Tie & Timber Company, and that no part of said mentioned sum has been paid except as shown by said annexed account, and no note has been taken therefor, and no judgment recovered on either of said debts, and that the said Western Tie & Timber Company has no security for either, other than as herein set forth, nor has any other person to its order.

WALTER POLEMAN.

STATE OF ARKANSAS, } ss:
*County of White,* }

Subscribed and sworn to before me this 15th day of May, A. D. 1903.

[L. S.] SAM J. CRABTREE,
*Notary Public.*

My commission expires July 6th, 1903.

5 (*Note S. F. Harrivon to Western Tie & Timber Co.*)

$22,154.26. POCAHONTAS, ARK, 1/16, 1903.

One day after date I promise to pay to the order of Western Tie & Timber Company, twenty-two thousand one hundred and fifty-four and 26/100 dollars, at St. Louis, with 6 % from date till paid, value received.

S. F. HARRISON.

*Statement of Account.*

S. F. Harrison to Western Tie & Timber Company, Debtor.

1903.

Jan. 16. To balance due for money loaned, after deducting amount for which note was given on that date, to wit: $22,154.26..... $5,570.00

Credits not deducted at giving of note because arising since note was given:

1903.

| | | |
|---|---|---|
| Jan. 21. | Deductions from pay-roll..... | $671.36 |
| Jan. 31. | Deductions from pay-roll..... | 357.34 |
| Feb. 19. | Deductions from pay-roll..... | 139.26 |
| | Total credits..... | $1167.96 |

Securities held:

| | |
|---|---|
| Saw mill taken under mortgage and title note, valued at and worth not exceeding..... | $1500.00 |
| 28 head of cattle, valued at, appraised at, and worth not exceeding..... | 428.00 |
| 13 hogs valued at, appraised at and worth not exceeding $7.50 each..... | 97.50 |
| 2 mules appraised at and worth not exceeding..... ..... .. | 175.00 |

| | | | |
|---|---|---|---|
| 6 | 1 two-horse plow, appraised at and worth not exceeding.... | 5.00 | |
| | 2 cultivators appraised at and worth not exceeding..... | 20.00 | |
| | 1 Buckeye mower, appraised at and worth not exceeding..... | 15.00 | |
| | 1 two horse plow, appraised at and worth not exceeding..... | 3.50 | |
| | 2 double-shovel plows, appraised at and worth not exceeding..... | 2.00 | |
| | 1 roller appraised at and worth not exceeding..... | 3.00 | |
| | 2 horses valued at and worth not exceeding..... | 60.00 | |
| | Total securities..... | ..... | $2309.00 |
| | Aggregate of credit deduction & securities..... | | $3,476.96 |
| | Balance due..... | ..... | $2,093.04 |

*(Motion of Trustee to Expunge Claim of Western Tie and Timber Company.)*

In the District Court of the United States for the Northern Division of the Eastern District of Arkansas.

*In re* S. F. HARRISON, Bankrupt. In Bankruptcy.

Comes Ben A. Brown, trustee herein and would respectfully show to the court that the Western Tie & Timber Company who have proved a claim against this estate have not proved their whole claim. But have only proved a part of the same, and have credited a large quantity of land, timber, cross ties and other property on the unproven part of their claim, and are thus obtaining a preference over other creditors. Wherefore this trustee prays that the claim of the Western Tie & Timber Company, proved against this estate, be expunged.

7

STUCKEY & STUCKEY,
H. L. PONDER, &
C. H. HENDERSON, *For Trustee.*

Indorsed: Filed April 17, 1903. Chas. F. Cole, referee.

(*Order of Submission.*)

And on the fourth day of January, A. D. 1904, in the record of the proceedings of said circuit court of appeals is an order of submission in said cause, in the words and figures following, to-wit:

United States Circuit Court of Appeals, Eighth Circuit, December Term, 1903.

MONDAY, *January* 4, 1904.

| | |
|---|---|
| WESTERN TIE AND TIMBER COMPANY, Appellant, *vs.* BEN A. BROWN, Trustee, &c. | No. 1953. Appeal from the District Court of the United States for the Eastern District of Arkansas. |

This cause having been called in its regular order on the merits, the same was argued by Mr. F. H. Sullivan in behalf of the appellant and by Mr. S. M. Stuckey for the appellee.

Thereupon the cause was submitted to the court on the merits, upon the transcript of record from said district court and the briefs of counsel filed herein.

(*Order to File Finding of Facts and Conclusions of Law.*)

And on the second day of April, A. D. 1904, in the record of the proceedings of said circuit court of appeals is an order in said cause to file the finding of facts and conclusions of law *nunc pro tunc* as of the date of the filing of the opinion, in the words and figures following, to-wit:

United States Circuit Court of Appeals, Eighth Circuit, December Term, 1903.

SATURDAY, *April* 2, 1904.

| | |
|---|---|
| 8 WESTERN TIE AND TIMBER Company, Appellant, *vs.* BEN A. BROWN, Trustee of the Estate of S. F. Harrison, Bankrupt, Appellee. | No. 1953. Appeal from the District Court of the United States for the Eastern District of Arkansas. |

On motion of F. H. Sullivan, counsel for the Western Tie & Timber Company, it is ordered, that the attached finding of facts and conclusions of law of this court be filed *nunc pro tunc* as of the

date of the filing of the opinion upon which the judgment of affirmance herein was based.

April 2, 1904.

(*Finding of Facts and Conclusions of Law.*)

The circuit court of appeals of the eighth judicial circuit finds these to be the facts in this case:

1. On February 24, 1903, a petition to procure an adjudication that S. Frank Harrison was a bankrupt was filed in the district court of the United States for the eastern district of Arkansas and Harrison was then adjudged a bankrupt.

2. The Western Tie & Timber Company was a corporation and a creditor of Harrison. It presented a claim against his estate in bankruptcy of $24,358. The trustee moved to expunge this claim on the ground that the tie company had secured a voidable preference. The district court ordered the claim expunged unless the tie company should pay to the trustee $2210.73 and an appeal from this order was taken to this court.

3. For some years prior to February 24, 1903, the tie company and Harrison had been engaged in removing timber from land of the former and converting it into ties which the company received and sold. For many months prior to October, 1902, Harrison had owned and conducted stores in the vicinity of the places where the work of cutting and hauling the ties was carried on and had furnished the laborers engaged in that work with groceries and other supplies. These laborers and Harrison were paid by the tie
9 company in this way: Once in two or four weeks an inspector sent to the tie company a pay roll on which the name of each laborer, the amount he had earned and the value of the supplies he had received from Harrison appeared. The company deducted from the earnings of each laborer the value of the supplies the laborer had received and sent him a check for the balance. At the same time it sent to Harrison a check for the aggregate amount of the supplies which he had furnished to the laborers.

4. Four months before the filing of the petition in bankruptcy or October 24, 1902, Harrison owed the tie company more than $20,000.

5. Between December 27, 1902, and February 24, 1903, the company refused to pay to Harrison, retained and credited on its claim against him $2210.73, which was due him for supplies he had furnished to the laborers subsequent to November 30, 1902.

6. At all times when the amounts which aggregate $2210.73 became due and were retained by the company Harrison was insolvent, the tie company knew that fact and it intended by retaining these amounts to secure to itself a preference over the other creditors of the insolvent, but Harrison had no such intention.

7. After the company had retained several hundred dollars of the

amount due Harrison for the supplies, it advanced to him $75 under a new and further credit.

And as conclusions of law the court finds:

A. The retention of the tie company of the $2210.73 constituted a voidable preference under the bankrupt law as amended.

B. The trustee is entitled to an order expunging the claim of the tie company unless that company pays to him the sum of $2135.73.

(Endorsed:) No. 1953. U. S. circuit court of appeals. 8th circuit. Western Tie & Timber Company, *vs.* Ben A. Brown, trustee &c. Findings of fact and conclusions of law. Filed by order of court Apr. 2, 1904, as of March 28, 1904, John D. Jordan, clerk.

10 (*Opinion.*)

And on the twenty-eighth day of March, A. D. 1904, an opinion of said circuit court of appeals was filed in said cause, in the words and figures following, to-wit:

11 United States Circuit Court of Appeals, Eighth Circuit, December Term, A. D. 1903.

| | |
|---|---|
| WESTERN TIE & TIMBER COMPANY, Appellant, *vs.* BEN A. BROWN, Trustee of the Estate of S. F. Harrison, Bankrupt, Appellee. | No. 1953. Appeal from the District Court of the United States for the Eastern District of Arkansas. |

Mr. F. H. Sullivan for appellant.

Mr. S. M. Stuckey (Mr. M. S. Stuckey and Mr. H. L. Ponder were with him on the brief) for appellee.

Before Sanborn, Thayer, and Hook, circuit judges.

*Syllabus.*

1. Bankruptcy—Transfer to preferred creditor not indispensable to preference under § 60*a*.—Under § 60*a* of the bankrupt law of 1898, as amended, a transfer of the debtor's property may constitute a preference although the property is not conveyed to the preferred creditor, if the effect of the transfer is to enable the creditor to receive out of the debtor's estate a larger percentage of his claim than others of the same class obtain.
2. Bankruptcy—Voidable preference—Intention of debtor to give, not indispensable.—An intention on the part of the insolvent to give a preference by means of a transfer he makes is not

indispensable to the existence of a voidable preference under § 60 of the bankrupt law, as amended, (32 Stat. 799). It is sufficient that a transfer of the insolvent's property is made which has the effect to give a preference and that the party who receives it has reasonable cause to believe that it is intended by the party who procures the transfer or who gives to the transfer the effect of a preference that it should have
12 that effect, although the insolvent is innocent of that intention.

3. Bankruptcy—Voidable preferences not allowable as offsets under § 68.—Preferences voidable under §§ 60*a* and 60*b* of the bankrupt law, as amended, are not allowable as setoffs against claims of the preferred creditors under § 68 on the ground that the preferences and the claims constitute mutual debts and credits.

4. Voidable preference—Facts.—A company was hiring laborers to gather ties. The insolvent was operating stores and supplying the men. For many months an inspector had sent a pay roll once in about two weeks to the company upon which the name of each laborer, his earnings and the amount furnished him by the insolvent, appeared. The company had uniformly deducted the price of the supplies from the earnings of each man, had sent him a check for the balance and had sent the insolvent a check for the supplies furnished. The insolvent owed the company more than $20,000, when, within four months of the filing of the petition in bankruptcy, it retained the amount owing the insolvent for the supplies furnished for three months and credited him with this amount, $2210.73, on its claim against him.

*Held*, this was a voidable preference and the claim of the company against the estate of the bankrupt should be expunged unless it pays to the trustee the amount it thus withheld.

SANBORN, circuit judge, delivered the opinion of the court:

This is an appeal from an order of the district court that the claim of the Western Tie & Timber Company against the estate of S. F. Harrison, a bankrupt, be expunged unless the company pays to the trustee the sum of $2210.73, which the court below found had been transferred to the company by the bankrupt in such a way that the transaction constituted a preference.

A motion has been made to dismiss the appeal under rule 11 of this court because the assignment of errors was not filed at the time of, or before the allowance of the appeal. The record, however, does not establish the fact upon which this motion is founded. The order allowing the appeal, the citation, the admission of service of the citation and the bond are dated June 12, 1903. The approval of the bond and the assignment of errors are not dated. All these papers were filed June 16, 1903. As the assignment of errors was

filed at the same time as the other appeal papers, the presumption is that it was presented to the court with them when the appeal was allowed, and the motion to dismiss is denied.

Harrison was adjudged a bankrupt on February 24, 1903. Prior to that time he owned some merchandise in two stores and he was engaged in forwarding the work of gathering ties from the lands of the tie company and in selling supplies to the laborers engaged in this work. Once in two or three weeks an inspector sent to the company a pay roll upon which the name of each workman, the amount owing to him for his services and the price of the supplies which Harrison had furnished him, appeared. The company uniformly deducted from the wages due each workman the price of the supplies Harrison had delivered to him, sent the workman its check for the balance and sent Harrison the price of all the supplies he had furnished to the laborers. This course of dealing had
13 been followed for many months on October 24, 1902, four months before the filing of the petition in bankruptcy. On that day Harrison owed to the company more than $20,000. He owed other creditors many thousand dollars. The tie company held a mortgage on his property to secure the payment of $15,000 to it and he was insolvent. During the month of December he applied to the tie company to advance him more money and it refused his request. Thereafter when the pay rolls for December, 1902, and January and February, 1903, came in, the company paid the laborers as usual, but instead of sending to Harrison as it had become accustomed to do, the price of the supplies which he had delivered to the men, it credited him with this amount which aggregated $2210.73, and in this way secured a payment of this amount upon its claim against him. The referee and the district court held that this transaction gave to the tie company a voidable preference and required it to pay to the trustee $2210.73 as a condition of the allowance of its claim against the estate of the bankrupt.

This ruling is challenged by counsel for the appellant on three grounds, because no transfer of anything by Harrison to the appellant was shown, because there was no proof that Harrison was insolvent or that the tie company had any notice of his insolvency when it withheld the price of the supplies and because there was no evidence that Harrison intended to prefer the tie company when he delivered the supplies to the men or that the company had any notice of any such intention.

But the test of a preferential transfer under the bankrupt act of 1898 is not whether or not the debtor has conveyed anything to the creditor, or whether or not the creditor has received anything from the debtor. It is whether or not the debtor has made a transfer of any of his property to anyone in any way whereby the enforcement of the transfer will enable one of his creditors to obtain a greater percentage of his debt than any other creditor of his class can secure. So the question in this case is not whether or not Harrison transferred any of his property directly to the tie company, but whether

or not any transfer of his property was made in the time and manner denounced by the bankrupt law so that the tie company was enabled to secure a larger percentage of its claim against him than other creditors of its class can obtain.

One of the main purposes of the bankrupt law is to distribute the unexempt property which the bankrupt has four months before the filing of the petition in bankruptcy, share and share alike, among his creditors. In order to attain this object the law provides that if a person, being insolvent, has, within four months before the filing of the petition, made a transfer of any of his property, the effect of the enforcement of which will be to enable anyone of his creditors to obtain a greater percentage of his debt than any other of his creditors of the same class, he shall be deemed to have given a preference, and that if he has given a preference and the person receiving it or to be benefited thereby, or his agent acting therein, shall have had reasonable cause to believe that it was intended thereby to give a preference, the claim of the creditor who has received such a preference shall not be allowed unless he surrenders it. §§ 60*a*, 60*b*, 57*g*, 32 Stat. 799, c. 487, §§ 12, 13; *Swartz v. Fourth Nat. Bank*, 117 Fed. 1, 3, 4, 54 C. C. A. 387, 389, 390. The uniform practice of the tie company for many months before October, 1902, to pay to Harrison once or twice in thirty days the price of all the supplies which he furnished to the workmen who prepared
14 and hauled the ties for it, warranted a finding and conclusion that while Harrison delivered the goods to the workmen he sold them to the tie company and that company became legally and morally bound to pay him their value. When, therefore, the company refused to pay him and credited him on account of these goods with $2210.73 upon its claim of $20,000 against him the effect of the transaction was to pay $2210.73 of Harrison's indebtedness to the tie company with these supplies which were a part of his estate. Moreover, whether the workmen or the tie company were the legal debtors of Harrison for these supplies, the actual result of the transaction was the same. Within the four months before the filing of the petition the supplies were a part of the estate of the insolvent Harrison. At the end of the four months they had been converted into ties which were a part of the property of the company. The latter had received in the ties the value of $2210.73 which had been transferred to it from the estate of Harrison and for which it had paid nothing to the workmen or to Harrison except by means of the credit it had given to Harrison upon its claim against him. But every transfer of his property by an insolvent within four months of the filing of the petition in bankruptcy which has the effect to "enable any one of his creditors to obtain a greater percentage of his debt" out of the property of the insolvent "than any other of such creditors of the same class" is a preference. *Swartz v. Fourth Nat. Bank*, 117 Fed. 4, 54 C. C. A. 390. The transfer of the supplies which were a part of the property of Harrison enabled the tie company to obtain about 10 per cent. more of its debt out of his estate

than other creditors of its class can secure, and the contention that this transaction did not constitute a preference under the law cannot be maintained.

Was Harrison insolvent when the company secured this preference and did the latter have notice of this fact? The answer must be in the affirmative. He owed the tie company more than $20,000. It held a mortgage on his property which had been made in January, 1902, to secure the payment of $15,000. He had frequently made statements of his assets and liabilities to the company which showed the former to be "a little bit more" than the latter. In December he applied for the advance of more money and the company refused his request because it had received information that his indebtedness was greater than he had represented it to be. Thereupon, on December 28, 1902, the company first applied an installment of its indebtedness to Harrison for the supplies furnished to its workmen to the payment of a part of the bankrupt's indebtedness to it. These facts convince that Harrison was insolvent and that the tie company knew it before it applied its indebtedness to him in payment of its claim against him.

There is no evidence in the record before us that Harrison ever intended by the sale of the supplies to prefer the tie company to his other creditors. Prior to December, 1902, the company had invariably sent him its checks for the supplies which he delivered and he probably expected that it would and intended that it should continue to do so. If it had done so, no preference would have been created. It failed to continue its practice and by withholding payment for the supplies from Harrison and crediting him with their price it secured a payment of $2210.73 upon its claim against him. Counsel for the company persuasively argue that this transaction did not constitute a voidable preference because Harrison did not intend to give any preference by means of it. But an intention on the part of the insolvent to give a preference by means of a transfer which he makes is not always indispensable to its existence. It is sufficient if he has given the preference and the party receiving it has reasonable cause to believe "that it was intended thereby to give" it. The statute does not require that it should be intended by the debtor, but is fully satisfied by the existence of an intention on the part of the actor, the person who procures, brings about or effects the transfer. The preferences denounced by the statute are often secured by creditors without any desire or intention on the part of the debtors to give them as in cases in which the creditors obtain judgments against their debtors over defenses made to the actions in good faith, and in cases, like that at bar, where, without the consent of their debtors, creditors appropriate to the payment of their claims the property of their debtors which happens to be under their control. Such transactions are none the less voidable preferences that the debtors do not intend them to have that effect. If they are conducted within the four months and if they have the effect to give to the creditors who con-

ceive and execute them larger percentages of their claims than other creditors of the same class receive, they fall as clearly under the ban of the law as transfers made by debtors with the intent on their part to give the preferences. Such a transaction is voidable by the trustee not only when the party receiving it has reasonable cause to believe that it was intended by the debtor but also when it was intended by the creditor, or by the actor who accomplished the result, to work a preference by means of the transaction. §§ 60*a*, 60*b*, 57*g*, 32 Stat. 799. The tie company in this case had reasonable cause to believe that the transaction which it conducted was intended to give it a preference over the other creditors of Harrison in its class. Indeed, it knew that this was the object of the transaction. It knew that its own intention and purpose was to secure such a preference by applying the debt it owed to Harrison for the supplies in part payment of its large claim against him for money advanced and it attained its object at least temporarily. The transaction fell fairly within the terms of § 60 and it constituted a voidable preference.

Finally, it is said that this $2210.73 was a credit to Harrison and that the company should be permitted to set it off against his debt to it and should be allowed to prove its claim for the balance remaining without restriction on the ground that these claims were mutual debts and credits under § 68 of the bankrupt law. But this section must be read and construed with sections 60*a*, 60*b* and 57*g* and in the light of the dominant purpose of the law to distribute to the creditors equally all the unexempt property owned by the insolvent four months before the petition in bankruptcy is filed. When it is thus read it becomes plain that preferences denounced by and made voidable under sections 60*a* and 60*b* cannot be permitted to stand as offsets against claims of the preferred creditors against the bankrupt which accrued more than four months before the filing of the petition. If this could be done, any creditor who had a running account with his debtor could secure an unassailable preference by simply receiving and crediting upon this account within the four months sufficient money or property of his debtor to satisfy his claim. The truth is that the law draws a line through the account between the insolvent and his creditor four months before the petition in bankruptcy is filed. All mutual debts and credits which accrue prior to that time may be set off against each other. Credits to the insolvent accruing subsequent to that time which constitute voidable preferences under section 60 are excepted by that section
16 from the subsequent provisions found in section 68 and they cannot be used to offset debts of the insolvent which accrue prior to that date. The mutual debts and credits which accrue within four months of the filing of the petition and which do not constitute voidable preferences may be set off against each other as well as against the respective debts and credits accruing more than four months before the petition is filed. The credit to Harrison of the $2210.73 constituted a voidable preference and cannot therefore be lawfully set off against the claim of the tie company against him

under section 68. There is, however, an item of $75 in the claim against Harrison which may perhaps properly be used to reduce the amount of the preference under section 60c, which provides that a claim for money or property delivered to a debtor under a new or further credit by a creditor after he has been preferred may be offset against the preference. While the evidence is not very satisfactory, it seems to indicate that this $75 was advanced to Harrison after the company had secured a preference to the amount of $1042.77. The amount to be refunded by it will accordingly be reduced by the sum of $75 and the order of the court below will be modified to the effect that the claim of the Western Tie & Timber Company against the estate of the bankrupt, Harrison, be expunged unless the company pays to the trustee of the estate $2135.73 within twenty days after the mandate of this court is filed and entered in the court below and the order thus modified will be affirmed. It is so ordered.

Filed March 28, 1904.

(*Decree.*)

And on the twenty-eighth day of March, A. D. 1904, in the record of the proceedings of said circuit court of appeals is a decree in said cause, in the words and figures following, to-wit:

17 United States Circuit Court of Appeals, Eighth Circuit, December Term, 1903.

MONDAY, *March* 28, 1904.

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| WESTERN TIE AND TIMBER COMPANY, Appellant, *vs.* BEN A. BROWN, Trustee of the Estate of S. F. Harrison, Bankrupt. | No. 1953. Appeal from the District Court of the United States for the Eastern District of Arkansas. |

This cause came on to be heard on the transcript of the record from the district court of the United States for the eastern district of Arkansas, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged and decreed by this court, that the order and decree of the said district court, in this cause, be, and the same is hereby, modified, to the effect that the claim of the Western Tie and Timber Company against the estate of the bankrupt, Harrison, be expunged unless that company shall pay to the trustee of the estate $2135.73 within twenty days after the mandate of this court is filed and entered in the court below, and that as thus modified, the order and decree of the said district court, in this cause, be, and the same is hereby, affirmed with costs; and that Ben A. Brown, trustee of the estate of

S. F. Harrison, bankrupt, have and recover against the Western Tie and Timber Company the sum of twenty dollars for his costs herein and have execution therefor.

March 28, 1904.

(*Petition for Appeal.*)

And on the fifteenth day of April, A. D. 1904, a petition for appeal was filed in the clerk's office of said circuit court of appeals in said cause, in the words and figures following, to-wit:

In the United States Circuit Court of Appeals for the Eighth Circuit.

18 WESTERN TIE & TIMBER COMPANY, Appellant, *vs.* BEN A. BROWN, Trustee of the Estate of S. F. Harrison, Appellee. } Number 1953.

*Petition for Appeal.*

The above named appellant conceiving itself *agrieved* by the judgment and decree made and entered in this cause by the United States circuit court of appeals for the eighth circuit on or about the 28th, day of March 1904, modifying and affirming the judgment and decree of the district court in this cause does hereby appeal from said judgment and decree to the Supreme Court of the United States for the reason specified in the assignment of errors which is filed and submitted herewith; and said appellant prays that its said appeal may be allowed and that a transcript of the record, proceedings and papers in this cause, and upon which said judgment and order was made, duly authenticated, may be sent to the Supreme Court of the United States.

F. H. SULLIVAN,
*Counsel for Appellant.*

The foregoing claim of appeal is hereby allowed, this the 13th day of April 1904.

WALTER H. SANBORN,
*Presiding Circuit Judge.*

(Endorsed:) Number 1953. In the United States circuit court of appeals for the eighth circuit. Western Tie & Timber Company appellant *vs.* Ben A. Brown, trustee of the estate of S. F. Harrison, appellee. Petition for appeal. Filed Apr. 15, 1904, John D. Jordan, clerk. F. H. Sullivan, lawyer, Carleton building, St. Louis, Mo.

19 (*Assignment of Errors.*)

And on the fifteenth day of April, A. D. 1904, an assignment of errors was filed in the clerk's office of said circuit court of appeals in said cause, in the words and figures following, to-wit:

In the United States Circuit Court of Appeals for the Eighth Circuit.

WESTERN TIE & TIMBER COMPANY, Appellant,
vs.
BEN A. BROWN, Trustee of the Estate of S. Frank Harrison, Appellee.
} Assignment of Errors.

Comes now Western Tie & Timber Company and says that the decree and judgment of the United States circuit court of appeals for the eighth circuit entered on March 28th, 1904 in the above entitled cause is erroneous and against its just rights for the following reasons, to-wit:—

First. Because the sale of supplies by the bankrupt to the employees of appellant was not a transfer of property by the bankrupt to appellant within the intent and meaning of the act of Congress relating to bankruptcy, such as to constitute a preference to appellant.

Second. Because the facts found by the United States circuit court of appeals show that appellant for some time prior to the adjudication had had in its employ persons to whom the bankrupt sold goods, and from the wages of such employees appellant deducted the amount due by the particular employé to the bankrupt and such acts did not constitute a transfer of property by the bankrupt as a preference within the meaning of the act of Congress relating to bankruptcy.

Third. Because on the facts as found by the United States circuit court of appeals, in selling goods to the employees of appel-
20 lant the bankrupt had no intention of preferring appellant over his other creditors, and under the act of Congress relating to bankruptcy as amended, without such intention on the part of the bankrupt his sale of goods to the employees of appellant did not constitute a voidable preference in favor of appellant.

Fourth. On the facts as found by the United States circuit court of appeals the act which that court holds to be a preference was the act of appellant in failing and refusing to pay to the bankrupt the amounts deducted from the wages of its employees on account of their indebtedness to the bankrupt and the failure and refusal of appellant to pay to the bankrupt the amount of such deduction, was not such an act as constitutes receiving or obtaining a prefer-

ence within the meaning of the act of Congress relating to bankruptcy.

Fifth. On the facts as found by the United States circuit court of appeals the act of appellant in deducting from the wages of its employees debts due by them to the bankrupt created an indebtedness in favor of the bankrupt against appellant for the amount of such deductions, and neither the failure nor refusal of appellant to pay these amounts to the bankrupt constituted the receipt of a preference by the appellant from the bankrupt within the meaning of the act of Congress relating to bankruptcy.

Sixth. On the facts as found by the United States circuit court of appeals the indebtedness of the bankrupt to appellant and the deductions by appellant from the wages of its employees on account of their indebtedness to the bankrupt constituted mutual debts and mutual credits within the intent and meaning of the act of Congress relating to bankruptcy and the aggregate of such deductions should have been set off against appellant's claim offered to be proven herein and the balance of said claim allowed against the estate.

Seventh. And for this, to wit, that by the record aforesaid
21 it appears that the judgment and decree aforesaid was given in favor of Ben A. Brown, trustee of the estate of S. Frank Harrison a bankrupt, whereas by the law of the land said judgment should have been given for said Western Tie & Timber Company and against the said Ben A. Brown trustee as aforesaid allowing the claim of said appellant as proven against the estate of said bankrupt, and said appellant Western Tie & Timber Company prays that the judgment of said United States circuit court of appeals for the eighth circuit modifying and affirming as modified the judgment herein of the district court of the United States for the northern division of the eastern district of Arkansas, may be reversed, annulled and held for naught as well as the judgment of the district court as so affirmed by the United States circuit court of appeals aforesaid and that appellant may be restored to all things lost by it by each and either of said judgments.

F. H. SULLIVAN,
*Attorney for Appellant.*

(Endorsed:) In the United States circuit court of appeals for the eighth circuit. Western Tie & Timber Company, appellant, *vs.* Ben A. Brown, trustee of the estate of S. Frank Harrison, appellee. Assignment of errors. Filed Apr. 15, 1904, John D. Jordan, clerk, F. H. Sullivan, lawyer, Carleton building, St. Louis, Mo.

(*Bond on Appeal.*)

And on the fifteenth day of April, A. D. 1904, an appeal bond was filed in the clerk's office of said circuit court of appeals in said cause, in the words and figures following, to-wit:

*Appeal Bond.*

Know all men by these presents, that the undersigned Western Tie & Timber Company a corporation under the law of the State of Arkansas as principal and the United States Fidelity & Guaranty Company a corporation under the law of the State of Maryland as surety, are held and firmly bound unto Ben A. Brown trustee
22 of the estate of S. F. Harrison a bankrupt, in the full and just sum of one thousand dollars ($1000.00) to be paid to the said Ben A. Brown trustee as aforesaid, his certain attorneys, executors, administrators, assigns or successor; to which payment will and truly to be made we bind ourselves and our successors jointly and severally by these presents.

Sealed with our seals and dated this the — day of April in the year of our Lord, one thousand nine hundred and four.

Whereas lately in the United States circuit court of appeals for the eighth circuit in a suit pending in said court between Western Tie & Timber Company, appellant, and said Ben A. Brown, trustee as aforesaid, appellee, a decree was rendered against the said Western Tie & Timber Company and the said Western Tie & Timber Company having obtained an appeal and filed a copy thereof in the clerk's office of the said court to reverse said decree, and a citation directed to the said Ben A. Brown trustee as aforesaid, citing and admonishing him to be and appear in the Supreme Court of the United States, to be holden at the city of Washington, within thirty (30) days from the date of said citation.

Now, the condition of the above obligation is such that if the said Western Tie & Timber Company shall prosecute said appeal to effect and answer all damages and costs if it fail to make good its said plea then the above obligation to be void, else to remain in full force and effect.

WESTERN TIE & TIMBER CO., [SEAL.]
By E. A. NIXON, *Vice Pres't.*

[SEAL.] THE UNITED STATES FIDELITY & GUARANTY CO.,
By PAUL W. GRAY, *Attorney in Fact.*

Approved April 13, 1904.

WALTER H. SANBORN,
*Circuit Judge.*

(Endorsed:) Western Tie & Timber Company, appellant, *vs.* Ben A. Brown, trustee of the estate of S. F. Harrison, appellee. Appeal bond. Filed Apr. 15, 1904, John D. Jordan, clerk. F. H. Sullivan, lawyer, Carleton building, St. Louis, Mo.

23 (*Citation.*)

And on the eighteenth day of April, A. D. 1904, a citation was filed in the clerk's office of said circuit court of appeals in said cause, the original of which, with the acceptance of service thereon, is hereto attached and herewith returned.

24 In the Supreme Court of the United States.

WESTERN TIE & TIMBER COMPANY, Appellant,
*vs.*
BEN A. BROWN, Trustee of the Estate of S. F. Harrison, Appellee.

UNITED STATES OF AMERICA, *Eighth Judicial Circuit*, } *ss:*

*Citation.*

To Ben A. Brown, trustee of the estate of S. F. Harrison, a bankrupt, Greeting:

You are hereby cited and admonished to be and appear at a session of the Supreme Court of the United States, to be holden at the city of Washington, within 30 days from the date hereof, pursuant to an appeal filed in the clerk's office of the United States circuit court of appeals for the eighth circuit, wherein Western Tie & Timber Company is appellant and you are appellee to show cause if any there be why the judgment rendered against the said appellant as in its petition for appeal set forth should not be corrected, and why speedy justice should not be done to the parties in that behalf.

Witness, the Honorable Melville W. Fuller, Chief Justice of the United States, dated this the 13th day of April in the year of our Lord, one thousand nine hundred and four.

WALTER H. SANBORN,
*Circuit Judge.*

25 Service of the foregoing citation is hereby accepted in behalf of the appellee Ben A. Brown, trustee of the estate of S. F. Harrison, this the 16 day of April 1904.

STUCKEY & STUCKEY AND
H. L. PONDER,
*Counsel for Appellee.*

26 [Endorsed:] In the Supreme Court of the United States Western Tie & Timber Company appellant *vs.* Ben A. Brown, trustee of the estate of S. F. Harrison, appellee United States of America eighth judicial circuit *ss.* Citation Filed Apr. 18 1904 John D. Jordan, clerk. F. H. Sullivan, lawyer, Carleton building, St. Louis, Mo.

27 (*Clerk's Certificate.*)

United States Circuit Court of Appeals, Eighth Circuit.

I, John D. Jordan, clerk of the United States circuit court of appeals for the eighth circuit, do hereby certify that the foregoing twenty-six pages contain full, true and complete copies of the order of reference; order of adjudication; proof of claim of Western Tie and Timber Company; note S. F. Harrison to Western Tie and Timber Company; statement of account; motion of trustee to expunge claim of Western Tie and Timber Company; order of submission to U. S. circuit court of appeals; order to file finding of facts and conclusions of law; finding of facts and conclusions of law; opinion of U. S. circuit court of appeals; decree of U. S. circuit court of appeals; petition for appeal; assignment of errors, and bond on appeal, in a certain cause wherein The Western Tie and Timber Company is appellant, and Ben A. Brown, trustee of the estate of S. F. Harrison, bankrupt, is appellee, No. 1953, December term, 1903, as full, true and complete as the same remain on file and of record in my office.

I do further certify that the original citation with acceptance of service thereon is hereto attached and herewith returned.

In testimony whereof, I hereunto subscribe my name and affix the seal of said circuit court of appeals, at office in the city of St. Louis, Missouri, in the eighth circuit, this twenty-first day of April, A. D. 1904.

[Seal United States Circuit Court of Appeals, Eighth Circuit.]

JOHN D. JORDAN,
*Clerk of the United States Circuit Court of Appeals for the Eighth Circuit.*

Endorsed on cover: File No. 19,307. U. S. C. C. of appeals, eighth circuit. Term No. 232. Western Tie and Timber Company, appellant, *vs.* Ben A. Brown, trustee of the estate of S. F. Harrison, a bankrupt. Filed April 23d, 1904. File No. 19,307.

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IN THE

# Supreme Court of the United States

October Term, 1904.

No. 282.

WESTERN TIE & TIMBER COMPANY, Appellant,

vs.

BEN A BROWN, Appellee.

## STATEMENT, BRIEF AND ARGUMENT FOR APPELLANT.

GEO. M. BLOCK,
F. H. SULLIVAN,
CHARLES BIRD,
For Appellant.

JOSEPH WHELESS,
Of Counsel.

IN THE

# SUPREME COURT OF THE UNITED STATES

October Term, 1904.

No. 232.

WESTERN TIE & TIMBER COMPANY, Appellant,

vs.

BEN A BROWN, Appellee.

Statement, Brief and Argument for Appellant.

## STATEMENT.

On the 24th day of February, 1903, on his voluntary petition to that end, S. Frank Harrison was adjudicated a bankrupt by the District Court of the United States for the Northern Division of the Eastern District of Arkansas (pr. 1-2), and the appellee, Ben A. Brown, is the acting trustee of his estate in that proceeding. Appellant, Western Tie & Lumber Company, proved a claim against the estate for money loaned, founded in part on the bankrupt's promissory note for $22,154.26, and partly on book account, on which latter a balance was

claimed to be due of $2,093.04, after crediting certain items among which were items termed "deductions from pay roll" (pr. 2-5). The trustee moved to expunge the entire claim on the ground that appellant had been the recipient of a preference from the bankrupt (pr. 5). This motion having prevailed in the District Court, appellant removed the cause by appeal into the United States Circuit Court of Appeals for the Eighth Circuit where a judgment was entered, March 28, 1904, modifying the judgment below and affirming it as modified, and directing that appellant's entire demand be expunged unless it surrendered to the trustee $2,135.73 (pr. 14). Appellant thereupon in due time filed its petition for appeal, its assignment of errors and bond and was allowed an appeal to this Court from the Circuit Court of Appeals (pr. 15-18), citation being issued and duly served (pr. 19).

The Circuit Court of Appeals, in accordance with the rule of this Court in that behalf, made and filed its finding of facts and conclusions of law (pr. 7-8) in which, after finding the adjudication and proof of appellant's claim, the order expunging it and the appeal therefrom hereinefore recited, it was found that for some months prior to the adjudication, appellant and the bankrupt had been engaged in removing timber from land owned by appellant and converting it into railway ties which appellant disposed of, and that the bankrupt had owned and conducted stores in the vicinity and furnished supplies to the laborers engaged in the manufacture and handling of the ties. Once in two or four weeks an inspector sent to appellant a pay roll showing the earnings of each laborer and the value of the supplies furnished him by the bankrupt. From such earnings appellant deducted the value of the supplies each laborer had received from the bankrupt, sent the laborer a check for the bal-

ance and at the same time sent the bankrupt a check for the aggregate amount of the supplies he had furnished the laborers. Four months before the filing of the petition in bankruptcy the bankrupt owed appellant more than $20,000.00. Between December 27th, 1902, and February 24th, 1903, appellant refused to pay the bankrupt $2.210.73 due him for supplies furnished to laborers subsequent to November 30th, 1902, and retained the same and credited it on its claim against him. When this occurred the bankrupt was insolvent and appellant knew the fact and "intended by retaining these amounts to secure to itself a preference," but the bankrupt had no such intention, and in the opinion of that court (pr. p. 12), it is shown that when the bankrupt delivered the goods he expected and intended to receive payment therefor from the appellant in accordance with the course of prior dealings between them. (A subsequent advance by appellant to the bankrupt of $75.00, not here involved, was also alluded to.)

As conclusions of law the Court found:

A. The retention by appellant of the $2,210.73 constituted a voidable preference under the bankrupt law as amended.

B. The trustee was entitled to have the claim expunged unless appellant surrendered $2,135.73 to the trustee, this amount being the amount so retained, less $75.00 found to have been subsequently advanced.

## SPECIFICATIONS OF ERROR.

In its assignment of errors (pr. 16-17) appellant specified errors as follows:

1. The sale of supplies by the bankrupt to the employes of appellant was not a transfer of property to appellant under the act, so as to constitute a preference.

2. The sale of supplies to such employes by the bankrupt and the deduction from their wages of the value thereof by appellant did not constitute a transfer of property by the bankrupt as a preference within the meaning of the Statute.

3. Because on the facts as found by the Circuit Court of Appeals the bankrupt had no intention to prefer appellant, and without such intention on his part his sale of goods to employes of appellant would not constitute a voidable preference in favor of appellant.

4. That which the Circuit Court of Appeals holds to be a preference was the act of appellant in failing and refusing to pay the bankrupt the sums deducted from the wages of its employes, on account of their indebtedness to the bankrupt, and the failure and refusal to pay such sums to the bankrupt was not receiving or obtaining a preference within the meaning of the act.

5. On the facts as so found the act of appellant in making these deductions from the wages of its employes, created an indebtedness from appellant to the bankrupt and neither the failure nor refusal to pay such indebtedness constituted obtaining or receiving a preference within the meaning of the Act.

6. On the finding of facts the indebtedness of appellant to the bankrupt because of such deductions, and the indebtedness of the bankrupt to appellant constituted mutual debts and mutual credits within the meaning of the act and should have been set off one against the other and the balance allowed against the estate.

## BRIEF.

### I.

This court has jurisdiction of this appeal upon the finding of facts and conclusions of law below.

Act of 1898, Section 25-b;
General Orders in Bankruptcy, XXXVI;
Pirie vs. Chicago Title & Trust Co., 182 U. S. 438;
New York County Bank vs. Massey, 192, Ib. 138.

### II.

The bankrupt had no intention to prefer appellant, and without such intention on his part there could be no preference arising from his sale of goods to appellant's employes.

Act of 1898, Section 57-g, as amended Feb. 5, 1903;
Ib. Section 60-b;
Act of 1841, Section 2;
(Act of 1867) Rev. Stat. U. S., Section 5128;
(Ib.) Ib. Section 5084;
Buckingham vs. McLean, 13 How. 169;
Wilson vs. City Bank, 17 Wall. 487;
Clark vs. Iselin, 21 Ib. 375;
Barbour vs. Priest, 103 U. S. 293;
Rice vs. Grafton Mills, 117 Mass. 228.

### III.

The sale of the supplies here in question, by the bankrupt, resulted in an indebtedness from appellant to him, was not payment of nor security for, appellant's

demand, and hence was not a preference, but a case of mutual debts to be set off, the one against the other.

Opinion of Circuit Court of Appeals, Pr. p. 11;
Hendrick vs. Lindsay, 93 U. S. 149;
Hecht vs. Caughron, 46 Ark. 132;
Century Digest Vol. II, Tit. Contracts, Sec. 798;
Act of 1898, Section 1 (25);
Ib. Section 68;
New York County Bank vs. Massey, *supra.*

## ARGUMENT.

### I.

This appeal from the Circuit Court of Appeals falls within subdivision b of Section 25 of the Act of Congress pertaining to bankruptcy in that the amount in controversy exceeds Two Thousand Dollars ($2,000.00) and the rights claimed by appellant for the allowance of its claim and for a set-off of the items, because of which it was expunged and the claim of the trustee that these items constituted a preference under the act, are asserted under the statutes of the United States, and hence there is presented a question within the jurisdiction of this Court upon writ of error to the highest courts of the States. Hence, also, in compliance with Rule XXXVI. of the General Orders in Bankruptcy the Circuit Court of Appeals was asked to, and did, file its finding of facts and conclusions of law, and the evidence upon which such findings were made up has been omitted from the transcript of the record brought to this Court.

The case of Pirie vs. Chicago Title and Trust Company, 182 U. S. 438, presented exactly the same situa-

tion as this case. There, as here, a claim had been allowed against the bankrupt estate, a motion filed to reconsider and disallow it, on the ground that the creditor had received a preference. The referee had so ordered. This ruling was reviewed and affirmed by the District Judge, an appeal was taken to the Circuit Court of Appeals, and upon its judgment of affirmance, the creditor asked and obtained its finding of facts and conclusions of law, and had his appeal allowed in that Court to this, and this Court accepted jurisdiction and disposed of the merits of the controversy.

The case of New York County National Bank vs. Massey, 192 U. S. 138, was another case where the trustee moved to expunge a claim which was offered for proof against the estate because of an alleged preference and an appeal was had upon findings of fact and conclusions of law from the Circuit Court of Appeals to this Court.

The terms of the Statute and the practical interpretation of it in the two cases referred to, seem to place beyond controversy the jurisdiction of this Court to review this decree in the manner in which it is here sought, and we therefore pass to the merits of the controversy.

## II.

The adjudication of bankruptcy in this case occurred February 24, 1903, and consequently the Act of 1898, with the amendments of February 5, 1903, control its disposition. Section 57-g of the Act, as thus amended, and as far as material here, reads as follows:

> "The claims of creditors who have received preferences *voidable under section sixty, subdivision b.* * * * shall not be allowed unless such creditors shall surrender such preferences."

The addition by the Act of February 5, 1903, being here quoted in italics.

This amendment was doubtless brought about by the decision of this court in Pirie vs. Chicago Title and Trust Company, *supra*, in which was pointed out the distinction, under the original enactment, between a preference simply, and a *voidable* preference (in the language of the amendment).

The Circuit Court of Appeals found as a fact that the bankrupt in this case had no intention to prefer appellant, and held that no such intention on his part was necessary to an order disallowing appellant's demand. Under the section just quoted, to deny proof of a claim because of a preference, the latter must be "voidable under section 60, subdivision b."

This statute provides:

> "If a bankrupt shall have given a preference and the person receiving it or to be benefitted thereby * * * shall have reasonable cause to believe *that it was intended thereby to give a preference*, it shall be voidable by the trustee," etc.

As stated, the Circuit Court of Appeals was of opinion that, under this statute, the intent necessary to avoid the transaction need not be held by the bankrupt, but might be held by the creditor alone, with the same resulting invalidity. In the Pirie case, as well as in the case of the New York County Bank, *supra*, this court pointed out the necessity of a plain interpretation of plain provisions of the Act, saying in the latter case that the courts are to interpret the statute, not to add to it. The language of this part of the Act requires that the creditor have reasonable cause to believe that it was thereby intended to *give* (not receive) a preference. That this language, according to its plain import, is only applicable to the in-

tention of the debtor, is self evident. The debtor *gives* a preference, the creditor *receives* one. The Court of Appeals applied the Act as though it provided for avoiding a preference as against any person "intending to receive a preference, or having reasonable cause to believe that the intention was to give such." It is respectfully submitted that this is not interpreting, but making, a statute, contrary to the rule of construction promulgated in the New York County Bank case. The illustration which the Court of Appeals adverted to—a preference obtained by judgment and execution, as furnishing proof of the fact that there might be a preference without such an intent on the part of the debtor—lends no support to the views advanced. Preferences obtained by legal process are controlled by section 67, subdivisions c and f, and under their terms all such are avoided by the adjudication *without reference to the intent of the debtor*, and indeed, in practical effect, without reference to the intent of the creditor, as well. Section 60 b, of the Act, has suffered no amendment since the original enactment, save with reference to the jurisdiction of the bankruptcy courts. The language of the Act on this question of intention stands now as it did at the beginning. And there is not, in the Act of 1898, such a departure in this regard from the language of earlier statutes, as to call for an interpretation upon the later Act, differing from that given those preceding. The inhibition in the Act of 1841 (Sec. 2) was against transfers "in contemplation of bankruptcy" and "for the *purpose* of *giving* * * * a preference."

In Buckingham vs. McLean, 13 How. 151, which arose under this statute, opinion by Mr. Justice Curtice, it was held, at page 168 et seq., that the acts forbidden could not be avoided without proof that the debtor contem-

plated his bankruptcy and *designed and intended* a preference.

The Act of 1867 contained similar provisions. Section 35 (Rev. St. Sec. 5128) avoided transfers "with a view to *give* a preference," while Sec. 23 (Rev. St. Sec. 5084) forbade a creditor receiving such a transfer to prove his claim.

In Toof vs. Martin, 13 Wall. 40, Mr. Justice Field delivered the opinion of the Court, and the entire language of the opinion on this question (page 48) shows that the intent of the *bankrupt* is the subject matter to be inquired about.

In Wilson vs. City Bank, 17 Wall. 473, at page 483 et seq., Mr. Justice Miller, in discussing these provisions of the Act of 1867, said:

> "What then is the true meaning of the act? In both cases it must be accompanied with an intent. In Section 35 it is to give a preference to a creditor. In Section 39 it must be to give a preference to a creditor or to defeat or delay the operation of the bankrupt act. In both there must be the *positive purpose* of doing an act forbidden by statute, and the thing described must be done in the promotion of this unlawful purpose."

In Clark vs. Iselin, 21 Wall. 360, at page 375, Mr. Justice Strong said, in discussing the question of preferences, under the Act of 1867:

> "The debtor must be insolvent, or contemplating insolvency, when the alleged preference is given, *and he must then have in view giving a preference.*"

It was also said, in that case, that the *bankrupt* must have "*a present intention to prefer a creditor*" to avoid a transfer. Of course, a requirement of reasonable cause

to believe in an intention to give a preference, by necessary implication requires the existence of such an intention, as one can not be said to have reasonable notice of a fact or condition, unless this fact or condition exists.

In Barbour vs. Priest, 103 U. S. 293, at page 296, Mr. Justice Miller said of a transfer under the provisions of the Act of 1867:

> "Such person (the grantee) must have reasonable cause to believe that the grantor in the conveyance was insolvent at the time it was executed, *and* that it was made with intent to defeat the bankrupt law. *Both these must exist* as facts which the grantee had reasonable cause to believe."

It is thus made to appear that the expressions, "for the purpose of giving a preference," in the Act of 1841, and "with a view to give a preference," in the Act of 1867, have been uniformly held to relate to the purpose and intention of the *bankrupt*. The difference between these former acts and the Act of 1898, lies merely in the substitution of the word "*intended*" in the later act. The significance is identical. And it must be taken that Congress had in mind the interpretation of the prior statutes, and intended the similar language of the present Act to receive a similar construction.

The case of Rice vs. Grafton Mills, 117 Mass. 228, involves the precise question here under discussion, upon facts strikingly similar. One Smith maintained a supply store, and the defendant, Grafton Mills, delivered to him a paper writing authorizing him to furnish its employes with money or supplies in amounts limited by the wages earned, and to render his account monthly to defendant for such advances. About the time he opened business the defendant loaned him a sum of money which it car-

ried in book account against him. For more than a year Smith supplied defendant's workmen and was paid by defendant monthly, for such supplies. Smith was adjudicated a bankrupt in October, 1870. Defendant retained and credited to him, on its demand, the value of the supplies furnished by him in July and August preceding, and the action was by his assignee to recover for such goods. There was evidence tending to show that the bankrupt was insolvent in July and August and that the defendant had reasonable cause to believe that such was the fact.

Smith testified that when he delivered the goods he expected the defendant to pay him for them, and did not know they were not going to do so until afterwards. The defendant requested a charge that if the bankrupt expected at the time he furnished the goods that defendant would pay him for them the verdict should be for the defendant. This the trial court refused, but charged that, if the defendant had the option to apply the goods to a pre-existing debt, and Smith was insolvent and knew it when he delivered the goods, the assignee could recover, notwithstanding the fact that Smith may have expected and supposed that he would be paid for the goods.

For the error in refusing the first request, and in giving the second, above summarized, the Supreme Judicial Court of Massachusetts reversed the judgment, holding that an intent to prefer was essential, and that *unless the bankrupt had such an intention when he delivered the goods there could be no recovery*, citing in support of its views, the opinion of this court in Toof vs. Martin, *supra*.

The finding of facts in this case shows that the bankrupt had no intention to prefer appellant, and consequently the Circuit Court of Appeals was in error in hold-

ing that there had been a voidable preference which appellant must surrender, as a condition precedent to proving its demand.

III.

The findings in this case are rather meager as to the relations of the parties with reference to supplies furnished by the bankrupt to the laborers. Whether the bankrupt had *carte blanche*, without limitation, to furnish such upon the direct responsibility of appellant; whether the liability of appellant was limited in each instance to the amount earned by the laborer supplied, or whether the liability of appellant for such supplies attached only when, with the consent of the particular laborer, the deduction had been actually made from his earned wages, is not made clear. It is immaterial, however, to ascertain which was the arrangement, because it is shown that appellant actually deducted the amounts under consideration from the wages of the laborers, and thereby, under either arrangement, its liability to the bankrupt for the aggregate of the amounts so deducted became fixed. The opinion of the Circuit Court of Appeals (Pr. p. 11) was that appellant became so liable to the bankrupt when the goods were sold. Be that as it may, it is certain that such a liability ultimately was established, and it seems clear that the bankrupt might have had his action of *indebitatus assumpsit* against appellant for the amount thereof. This was clearly the view of the Circuit Court of Appeals and is supported by the decision of this court in Hendrick vs. Lindsay, 93 U. S. 143, to the effect that appellant's deductions implied a promise to pay the bankrupt. And the rule prevailing in Arkansas, where these matters arose, is that a promise to one for the benefit of another gives a right of action upon such promise to the person for whose benefit it is made

(Hecht vs. Caughron, 46 Ark. 132); and such is the overwhelming current of American authority. See Century Digest, title "Contracts," Section 798, where the decisions on this subject are collated. Upon any view of the facts there was implied from the course of dealings prevailing, a promise on the part of appellant to pay the bankrupt the amounts deducted from the wages due its employes. In other words, and, in any event, upon the making of the deductions, appellant became indebted to the bankrupt therefor, and the relations of the parties were then that of debtor and creditor, inasmuch as the finding of facts negatives the possibility that the bankrupt made the sales, intending them as a payment on his indebtedness to appellant. This is shown by the conclusions of law announced below (Pr. 8) to the effect that it was the retention of these deductions which constituted the voidable preference. In other words, the preference, according to the view below, was *the failure and refusal to pay a debt*. Upon these facts the case of *New York County National Bank vs. Massey, supra*, is controlling authority and establishes that under a proper construction of the act, the case presented is that of mutual debts, to be set off one against the other, rather than a case of a preference. In that case the bankrupts were indebted to the bank upon sundry bills, and also maintained a general deposit account with it. The adjudication was on January 27th, and they made deposits of different amounts to their credit, on the 22nd, 23rd and 25th of the same month. One, at least, of these was after the bank had notice of their insolvency. The bank applied the balance standing to the credit of the bankrupt, on account of these deposits, to the payment of the bills, and offered to prove its claim for the resulting balance in its favor. The Circuit Court of Appeals for the Second Cir-

cuit, held these facts to show a preference. It was contended in that Court that under the terms of Section 1 (25) of the Act, the transfer of these funds was not a preference, because neither a payment, pledge, mortgage, gift, or security, but that Court was of opinion that these words in the definition of a transfer were merely by way of illustration and not of limitation (116 Fed. 342). Upon a finding of facts by that Court, the cause was brought here by appeal, and this Court reversed the judgment of the Circuit Court of Appeals, and affirmed that of the District Court allowing the claim. The two sections of the Act which were particularly involved were Section 1 (25), reading as follows:

> "Transfer shall include the sale and every other and different mode of disposing of or parting with property or the possession of property, absolutely or conditionally, *as a payment, pledge, mortgage, gift or security.*"

And section 68 of the Act, reading as follows:

> "In all cases of mutual debts or mutual credits between the estate of a bankrupt and a creditor, the account shall be stated and one debt shall be set off against the other, and the balance only shall be allowed or paid."

The opinion of this court, by Mr. Justice Day, may be briefly summarized as follows:

1. Section 1 (25) must be read with sections 57-g and 60-a, and no transaction is a preference which is not either payment, pledge, mortgage, gift or security.

2. The deposits in the bank created an equivalent indebtedness from the bank to the depositor, and hence worked no diminution of the estate of the depositor.

3. There were mutual debts between the bankrupt and the bank, on account of these bills payable and de-

posits, which, under the terms of Section 68, should be set off one against the other.

It was said in that case:

> "We are to interpret statutes, not to make them. Unless other sections of the law are controlling, or, in order to give a harmonious construction to the whole act, a different interpretation is required, it would seem clear that the parties stood in the relation defined in Sec. 68-a, with the right to set off mutual debts, the creditor being allowed to prove but the balance of the debt."
>
> * * * * * * *
>
> "But it is urged that under Sec. 60-a this transaction amounts to giving a preference to the bank, by enabling it to receive a greater percentage of its debts, than other creditors of the same class. A transfer is defined in Sec. I (25) of the act to include the sale and every other and different method of disposing of or parting with property or the possession of property, absolutely or conditionally, as a payment, pledge, mortgage, gift, or security. While these sections are not to be narrowly construed so as to defeat their purpose, no more can they be enlarged by judicial construction to include transactions not within the scope and purpose of the act. This section, I (25), read with Secs. 57-g, and 60-a, requires the surrender of preferences having the effect of transfers of property 'as payment, pledge, mortgage, gift, or security which operate to diminish the estate of the bankrupt and prefer one creditor over another.'"
>
> "The law requires the surrender of such preferences given to the creditor within the time limited in the act before he can prove his claim. These transfers of property, amounting to preferences, contemplate the parting with the bankrupt's property for the benefit of the creditor, and the consequent diminution of the bankrupt's estate.

It is such transactions, operating to defeat the purposes of the act, which, under its terms, are preferences."

"As we have seen, a deposit of money to one's credit in a bank does not operate to diminish the estate of the depositor, for when he parts with the money he creates at the same time, on the part of the bank, an obligation to pay the amount of the deposit as soon as the depositor may see fit to draw a check against it. It is not a transfer of property as a payment, pledge, mortgage, gift, or security. It is true that it creates a debt, which, if the creditor may set it off under Sec. 68, amounts to permitting a creditor of that class to obtain more from the bankrupt's estate than creditors who are not in the same situation, and do not hold any debts of the bankrupt subject to set-off. But this does not, in our opinion, operate to enlarge the scope of the statute defining preferences so as to prevent set-off in cases coming within the terms of Sec. 68-a. If this argument were to prevail, it would, in cases of insolvency, defeat the right of set-off recognized and enforced in the law, as every creditor of the bankrupt holding a claim against the estate subject to reduction to the full amount of a debt due the bankrupt receives a preference in the fact that, to the extent of the set-off, he is paid in full."

The parallel between that case and this is well-nigh perfect. There, as here, the transfer was not payment, pledge, mortgage, gift, or security; there, as here, the transfer resulted in creating an indebtedness to the bankrupt equivalent to the thing transferred and hence resulted in no diminution of the bankrupt's estate; there, as here, the actual preference resulted from the set off of mutual debts, which, as was said by this Court, *supra*, is a necessary result of the enforcement of Section 68 of the Act.

The opinion of this Court in the *New York County Bank* case, while promulgated, had not been published, when this case was determined in the Circuit Court of Appeals, and hence was not presented to that Court, otherwise this appeal would, probably, have been unnecessary, as the opinion in that case seems clearly to control this one, and to require the reversal of the judgment of the District Court and of the Circuit Court of Appeals, and the remand of the cause with directions to allow appellant's demand against the estate.

Respectfully submitted,

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CHARLES ERD,
For Appellant.

JOSEPH WHELESS,
Of Counsel.

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—IN THE—

# SUPREME COURT OF THE UNITED STATES.

## OCTOBER TERM, 1904.

## No. 232.

WESTERN TIE AND TIMBER CO., APPELLANT,

*vs.*

BEN A. BROWN, TRUSTEE, APPELLEE.

STATEMENT, BRIEF AND ARGUMENT FOR THE APPELLEE.

C. F. HENDERSON,
H. L. PONDER,
M. M. STUCKEY,
S. M. STUCKEY,
For Appellee.

JOHN M. MOORE,
Of Counsel.

HERALD PRINTING CO. NEWPORT.

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## STATEMENT, BRIEF AND ARGUMENT FOR THE APPELLEE.

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### STATEMENT.

The record in this case is very short, and the facts are all in the Transcript of Record, pages 7 and 8, so it is unnecessary to repeat them here.

### BRIEF.

I.

This Court does not have jurisdiction of this appeal.

Hutchinson vs. Otis, 123 Fed. 14.

Denver National Bank vs. Klug, 186 U. S. 202.

Holden vs. Stratton, 191 U. S. 115.

Wherefore appellee asks that the appeal be dismissed.

II.

An intention on the part of the bankrupt to give a preference by means of a transfer he makes is not indespensible to the existance of a voidable preference.

Bankruptcy Act of 1898, Sections 60a, 60b, 57g, 32 Stat. 799.

Chap. 487, sections 12, 13.

Collier on Bankruptcy (4th Ed.) pages 387, 388, 389 and 537.

Swarts vs. Fourth National Bank 117 Fed. 1, 3, 4, 54 C. C. A. 387-89-90.

Opinion of Circuit Court of Appeals, Tr. p. 11.

III.

The sale of supplies by bankrupt to the laborers and the appellant deducting the amounts of them from the pay rolls and retaining same did not create an indebtedness from appellant to bankrupt, but was a voidable transfer of bankrupt's property and a preference, and was not a case of mutual debts to be set off the one against the other.

Act of 1898, Sec. 1, definition No. 25.

1b Sections 60a, 60b and 68.

In re Christainsen 101 Fed. 802.

In re Ryan 105 Fed. 760.

Libby vs. Hopkins 104 U. S. 303.

In the matter of Tacoma Shoe & Leather Co. 3 Nat. B. N. & Rep. 9.

Sawyer vs. Hoag 84 U. S. 610-22.

## ARGUMENT.

In the cases cited by appellant as authority for this Court to assume jurisdiction of this cause, the question of jurisdiction was not raised or discussed, hence those cases are not authority on that point. From all that appears in the reports of the Pirie case and the New York County Bank case, cited by appellant, those cases might have reached this Court because the appeal was granted by one of the Justices of the Supreme Court. If that was done, then the Court had jurisdiction; but that could only be determined by an examination of the files in those cases, and that we have not had the opportunity of doing.

To take an appeal or writ of error from the Supreme Court of the State to the Supreme Court of the United States, it is not sufficient that an Act of Congress is to be construed, but a right must have been claimed under it which was denied by the State Court.

Rev. Stat. 709.

The cases cited by appellant in its brief are not in point, and most of them arose under acts substantially different from the one we are considering and are inapplicable, hence we shall not enter into a detailed discussion of the several cases cited. There is one, however, we shall note in passing and that is New York County Bank vs. Massey, 192 U. S. 138, because counsel seem to rely upon it to support their contention; but our reading of that case convinces us that it has no application to the case at bar whatever. The only point decided in that case is that a bank can set-off the amount it has deposited with it against a debt owing to it from its depositor. That case was correctly decided because a bank has a lien upon the balance of a general deposit account for all indebtedness due to it

from the depositor and for the further reason that the depositing of money in a bank subject to be checked out does not work a diminution of the assets of the depositor but such deposit is itself an asset.

It should be borne in mind that appellant in this case is not a bank.

It is true that the petition for the adjudication in bankruptcy was filed on the 24th day of February, 1903, and it is probably true that this cause must be determined by the amended act which was approved February 5th, 1903, although there is a case, in re Busby 124 Fed. 469 l. c. 471, which seems to hold that the law as it stood when the property was turned over is to govern.

The contention of the appellant in a great measure, as we take it, grows out of its misconstruction given to section 60 sub-div. b, in that it contends that the intention on the part of the bankrupt to give a preference must appear. While we believe only a reasonable cause to believe a preference was intended must appear and no further notice to the creditor than reasonable cause to believe is necessary.

We also differ from counsel for appellant as to what is really meant by a transfer. They seem to think the retaining of money due to the bankrupt on the store accounts was not a transfer of his property, while we think it was.

Nor do we think the facts in this case establish a case of mutual debts to be set off against each other. This is probably one of the first cases to reach this Court under the amendatory act of February 5th, 1903, and as precedents are lacking, this case must be decided on principle. We must constantly keep in mind the purpose and intendment of this entire law, which is

to distribute the unexempt property which the bankrupt has four months before the filing of the petition in bankruptcy, share and share alike, among his creditors. Only by doing this can justice be done. It is true the Court should give effect to all parts of the act if possible, but should not adopt a strained construction of the whole act to give effect to the doubtful wording of a single section.

"The letter killeth, but the spirit giveth light." —2 Cor. 3-6.

A transfer is defined in the act itself, Chap. 1, page 15, defination No. 25: "Transfer shall include the sale and every other and different mode of disposing of or parting with property, absolutely or conditionally, as a payment, pledge, mortgage, gift or security." In view of this definition in the very law itself, it could hardly be argued that the retaining money due to the bankrupt on the store accounts, for supplies sold and delivered by the bankrupt to the laborers, was not a transfer of his property. In Pirie vs. Chicago Title & Trust Co. 182 U. S. 438, definition No. 25 was given a very broad application, even more so than we are contending for here.

It is now settled beyond controversy that at the time of these transfers the appellant company knew that Harrison was insolvent and intended by retaining these amounts to secure to itself a preference over the other creditors of the insolvent. Tr. p. 7. Finding of Fact No. 6.

There can be no question either but that the appellant by retaining these amounts for supplies within the four months prior to the filing of the petition obtained a preference because the effect of so doing

was to enable it to secure a greater per cent of its debt than any other creditor of the same class. Sec. 60a.

Collier on Bankruptcy (4th Ed.) at page 387 in treating of Sec. 57 sub-div. g of the original act says:

"Preference claims. Sub Sec. 8 has been as much discussed as any clause in the present law. The former statute denied allowance to any claim filed by a creditor who accepted a preference, 'having reasonable cause to believe that the same was made or given by a debtor contrary to the provisions of the act,' nor could any dividend be paid on such a debt until the creditor had surrendered his advantage. The words quoted do not appear in the (original of) the present act. Further the defination of preference was by shifting of clauses, while the bill was in committee so changed as to lead to the ruling that any payment by debtor or creditor after, though without actual knowledge of insolvency, was a preference, even though lacking in intent, and made years before.

Pirie vs. Chicago Title & Trust Co., 182 U. S. 438, settled the matter. After it all payments subsequent to insolvency were preferences, the surrender of which was required before the the claim of the creditor so preferred could be allowed."

Again Collier on Bankruptcy, (4th. Ed.) 388. "The amendment of 1903. The conditions resulting from the new doctrine—a reversal of the settled policy of all bankruptcy laws to protect the transactions in due course, even up to the moment of bankruptcy—were so unsatisfactory to business men and disastrous to the creditors that the demand for remedial legislation was practically unanimous. Congress has responded by amendments (1) making it certain that no transaction more than four months before the bankruptcy is a

preference; and (2) limiting that which must be surrendered as a condition prescedent to proving a debt to (a) preferences that are voidable under Section 60, sub-div. b; and (b) advantages possessed by creditors to whom conveyances, transfers, assignments or incumbrances void or voidable under Section 57 sub. div. e have been made or given."

"Meaning of the amendments. Considered broadly, sub-section g seems now to mean what the 'protected transactions' clauses of the English system have meant for nearly two centuries. He who has obtained an advantage over his creditors in any of the ways indicated in the present law, and only such as one must hereafter surrender his advantage before his claim can be filed or allowed."

Again, on page 389 he says: "Amendments in actual practice. The effect of the change in section 57 g will be to limit objections to the allowance of claims on the ground of preference to such transactions as are void or voidable under Section 60b or 67e." And further on he says: "If not voidable under Section 60b a preference need not be surrendered. Reasonable cause to believe a preference must appear; an intention to prefer need not," and thus it is written, Section 60b, "If a bankrupt shall give a preference, and the person receiving it or to be benefited thereby, or his agent acting therein, shall have reasonable cause to believe that it was intended thereby to give a preference, it shall be voidable by the trustee, and he may recover the property or its value from such person."

Now in order to arrive at as to whether this action comes under the ban of the law, we take Sec. 60a and Sec. 60b together. Section 60a defines a preference as follows: "Person shall be deemed to have given a

preference if being insolvent, he has within four months before the filing of the petition made a transfer of any of his property, and the effect of such transfer will be to enable any one of his creditors to obtain a greater percentage of his debt than any other of such creditors of the same class." There is no dispute as to the insolvency, nor as to the time when the credits were made as being within four months. It is also obvious that to permit appellant to retain these amounts, the effect will be to enable it to obtain a greater percentage of its debt, than other creditors of the same class, and under the finding of facts it is now beyond dispute that appellant had reasonable cause to believe a preference intended. We thus find the transaction under the ban of every clause of the law and unquestionably voidable.

Collier on Bankruptcy, 4th ed., page 537, says:

Effect of amendment on preferences:—"It follows from what has already been said before, that 57g, being one of administration only, the new rule, i. e., the reverse of Pirie vs. Chicago T. & T. Co., 182 U. S. 438 will apply to all cases begun after February, 1903. The changes in sections 60a and 60b, are largely those of transposition, only in re Dilling, 124 Fed. 852, the ruling in the Pirie case is followed, and incidentally it is held that the reverse would be the rule in cases arising since the amendment."

In the case at bar there was an attempt to substitute debtors, with the intent, as the Court of Appeals found, to prefer it to other creditors; there was no debt in fact due from the apellant to the bankrupt. And it may be explained in this way, the appellant was indebted to certain laborers for making, rafting and hauling ties, the amount of which was shown in the bi-weekly statement sent to the appellant by the bankrupt. This

statement also showed the amount of supplies sold by the bankrupt on a credit to the laborers, when the checks were to be sent by the appellant to the laborers for the amount of their services, the appellant first deducted the amounts due from the several laborers to the bankrupt and forwarded a check for the difference with the implied promise to the laborers that it would turn over the difference to the bankrupt in payment of the debt owing by the laborers for supplies to the bankrupt. Now this was not a debt owing by the appellant to the bankrupt, on which he could maintain an action if the appellant failed to turn over to the bankrupt in payment of the laborers' debts, and the bankrupt could only have this action against the laborers, who were his real debtors, and not against the appellant, who was the debtor of the laborers, and only held these several sums in trust for the laborers, to be turned over to the bankrupt. This does not constitute the transaction then, between the bankrupt and the appellant, mutual debts which could be set off one against the other.

The principle involved, in re Christainsen, 101 Fed. 802, we believe control here, There it is held that a payment of money to apply upon a debt, is a transfer of property and if made by an insolvent debtor with the effect of enabling the creditor to obtain a greater portion of his debt thrn the other creditors constitutes a preference. And that where a trustee in bankruptcy opposes the allowance of a claim filed by a creditor based upon an open account for goods sold by him to the bankrupt, on the ground that the creditors has received preferences, which he has not surrendered in the way of payment to apply on such accounts, the creditor cannot set off against the trustee's demand for the surrender of such preferences the amount due for goods sold, such a case not being one of mutual debts or mu-

tual credits between the estate of a bankrupt and a creditor. To the same effect is

In re Rryan, 105 Eed. 760.

In Libby vs. Hopkins 104 U. S. 303, the doctrine of set off is discussed. In that case the facts were that one person was indebted to another by a note secured by mortgage annd on an account. The first person sent the second person money with instructions to ap ply it on the note. Shortly thereafter the first person was adjudged a bankrupt. It was held that the money was received by the second person in trust to apply it persuant to instructions, and having refused to conform to them, he could not set it off against the account, but was liable therefor to the assignee in bankruptcy of the first person. Further on in the decision "the refusal of the person to apply them according to instructions did not change the relation of the parties to this fund. It did not make that a "debt" which before such refusal was a trust. To so hold would be to permit a trustee to better his condition by a refusal to execute a trust which he has assumed," and further on they say, "in our act 1867, the term credit and debts are used as correlative. What is a debt on one side is a credit on the other, so that the term credits can have no broader meaning than the term debts. We find no warrant in the language of the section or its context for extending the term credits so as to include trusts. Generally we know that credits and trusts are not synonomous terms. They have distinct and well settled meanings. To authorize a set off there must be mutual credits or mutual debts.

And our contention here, is that the appellant never did owe the bankrupt anything, hence there could be no mutual debts. So there could be no set off.

In Sawyer vs. Hoag 84 U. S, 610 is a case involving the doctrine of set off. At page 622 the court said: "The debts must be mutual; must be in the same right."

Can it be said from the facts in this case that the debts in the case at bar were mutual, and in the same right! We think not. The laborers owed the bankrupt and the appellant owed the laborers. These amounts were held by the appellant under the implied promise to the laborers to pay them to the bankrupt to be applied on certain accounts. As we take it, the appellant held it in trust, and not as a mutual debt owing by it to the bankrupt.

In the matter of the Tacoma Shoe & Leather Co. 3 Nat. B., News & Rep. 9, is a case that seems to be in point. In this case a trustee filed a petition asking for an order against the Fidelity Trust Co., a bank, asking it to show cause why it should not surrender certain sums of money had on deposit by it at the time the trustee took charge, and a further sum alleged by the trustee to have been collected by it upon a draft deposited with it for collection. The bank answered and pleaded that the bankrupt owed it a certain note and interest, and sought to set off, one against the other. The transfer in this case was made after the adjudication in bankruptcy. The Court held that notice of insolvency, under section 68, was a bar to a counter claim. In this case it was held that a set off, or counter claim, could not be allowed on favor of any debtor of the bankrupt, which was transferred to him after the filing of the petition or within four months before such filing, with knowledge or notice that such bankrupt was insolvent or had committed an act of bankruptcy.

As before remarked, the appellant had full notice of the insolvency of the bankrupt Harrison, in the case

at bar, during all the time covered by the transactions in question here.

With the four months before the filing of the petition the supplies were a part of the estate of the insolvent Harrison. At the end of the four months they had been converted into ties, which were a part of the property of the appellant company. The latter had received in the ties the value of $2,210.73, which had been transferred to it from the estate of Harrison, and for which it had paid nothing to the workmen or to Harrison, except by means of the credit it had given to Harrison upon its claims against him. But every transfer of his property by an insolvent, within four months of the filing of the petition in bankruptcy, which has the effect to enable any one of his creditors to obtain a greater percentage of his debt out of the property of the insolvent than any other of such creditors of the same class, is a preference. The transfer of the supplies which were a part of the property of Harrison enabled the Tie Company to obtain about 10 per cent more of its debt out of his estate than other creditors of its class and thus obtain for itself a preference.

The law draws a line through the account between the insolvent and his creditors four months before the petition in bankruptcy is filed. All mutual debts and credits, which accrue prior to that time, may be set off against each other. Credits to the insolvent, accruing subsequent to that time which constitute voidable preferences, under section 60, are excepted by that section from the subsequent provisions, found in section 68, and they can not be used to offset debts, which accrue prior to that date.

Under the facts in the case at bar, we contend that there was a voidable preference obtained by the appellant, and that the same cannot be used as an offset.

We, therefore, respectfully submit that this Court has not jurisdiction of this case and this appeal should be dismissed, but should the Court hold otherwise, we submit that the finding of the Referee and the decree of the District Court, as modified and affirmed by the Circuit Court of Appeals for the Eighth Circuit, is cor rect and should in all things be affirmed, together with cost, for which we ever pray.

Respectfully submitted,

C. F. HENDERSON,
H. L. PONDER,
M. M. STUCKEY,
S. M. STUCKEY,
For Appellee.

JOHN M. MOORE,
Of Counsel

# Supreme Court of the United States.

No. 232.—October Term, 1904.

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| Western Tie and Timber Company, Appellant, *vs.* Ben A. Brown, Trustee of the Estate of S. F. Harrison, a Bankrupt. | Appeal from the United States Circuit Court of Appeals for the Eighth Circuit. |

[February 20, 1905.]

This is an appeal from a decree of the Circuit Court of Appeals for the Eighth Circuit, affirming, as modified, an order of the District Court of the United States for the Eastern District of Arkansas, directing that the claim of the Western Tie and Timber Company against the estate of S. F. Harrison, a bankrupt, be expunged, unless the company paid to the trustee in bankruptcy a specified sum, found to have been transferred to the company by the bankrupt and decided to have operated a voidable preference. (129 Fed. Rep. 728.)

The facts were thus found by the Circuit Court of Appeals:

"1. On February 24, 1903, a petition to procure an adjudication that S. Frank Harrison was a bankrupt was filed in the District Court of the United States for the Eastern District of Arkansas, and Harrison was then adjudged a bankrupt.

"2. The Western Tie and Timber Company was a corporation and a creditor of Harrison. It presented a claim against his estate in bankruptcy of $24,358. The trustee moved to expunge this claim on the ground that the tie company had secured a voidable preference. The District Court ordered the claim expunged unless the tie company should pay to the trustee $2,210.73, and an appeal from this order was taken.

"3. For some years prior to February 24, 1903, the tie company and Harrison had been engaged in removing timber from land of the former and converting it into ties, which the company received and sold. For many months prior to October, 1902, Harrison had owned and conducted stores in the vicinity of the places where the work of cutting and hauling the ties was carried on, and had furnished the laborers engaged in that work with groceries and other supplies. These laborers and Harrison were paid by the tie company in this way: Once in two or four weeks an inspector sent to the tie company a pay roll, on which the name of each laborer, the amount he had earned and the value of the supplies he had received from Harrison, appeared. The company deducted from the earnings of each laborer the value of the supplies the laborer had received and sent him a check for the balance. At the same time it sent to Harrison a check for the aggregate amount of the supplies which he had furnished to the laborers.

"4. Four months before the filing of the petition in bankruptcy, or October 24, 1902, Harrison owed the tie company more than $20,000.

"5. Between December 27, 1902, and February 24, 1903, the company refused to pay to Harrison, retained and credited on its claim against him $2,210.73, which was due him for supplies he had furnished to the laborers subsequent to November 30, 1902.

"6. At all times, when the amounts which aggregate $2,210.73 became due and were retained by the company, Harrison was insolvent, the tie company knew that fact, and it intended by retaining these amounts to secure to itself a preference over the other creditors of the insolvent, but Harrison had no such intention.

"7. After the company had retained several hundred dollars of the amount due Harrison for the supplies, it advanced to him $75 under a new and further credit."

An appeal to this court was allowed by the presiding circuit judge of the Circuit Court of Appeals.

Mr. Justice WHITE, after making the foregoing statement, delivered the opinion of the Court.

Before coming to the merits we dispose of an objection to the jurisdiction.

The appeal was prosecuted under clause (*b*) 1 of section 25 of the bankrupt act of July 1, 1898, (30 Stat. at L. 553,) providing that from any final decision of a Court of Appeals, allowing or rejecting a claim under the act, an appeal may be had "where the amount in controversy exceeds the sum of two thousand dollars, and the question involved is one which might have been taken on appeal or writ of error from the highest court of a State to the Supreme Court of the United States."

The provision of the Revised Statutes regulating the revision of judgments and decrees of State courts, which is relied upon, in conjunction with the portion of the bankruptcy act just quoted, is that portion of section 709, which authorizes the re-examination of a final judgment or decree in any suit in the highest court of a State in which a decision in the suit can be had, "where any title, right, privilege or immunity is claimed under . . . any . . . statute of . . . the United States, and the decision is against the title, right, privilege or immunity specially set up or claimed, by either party, under such . . . statute, . . ."

The appellee does not question that this appeal is from a decree rejecting a claim, within the meaning of the statute, and that the requisite jurisdictional amount is involved, but the particular objection urged is that a right was not claimed under an act of Congress, nor was a right of that nature denied by the lower courts.

The objection is not tenable. It clearly appears from the record that in the claim filed on behalf of the tie company there was embodied, as an

integral part thereof, as a proper credit or set-off, the sum retained from the wages of employees for supplies furnished by the bankrupt, and the rejection of the claim was based upon the denial of the right to set-off. As the right of set-off is controlled by the provisions of section 68 of the bankrupt act, the assertion of such a right, in a proceeding in bankruptcy, as was the case here, is necessarily based upon those provisions of the act of Congress, and in this case the construction of such statutory provision was undoubtedly involved. That the Circuit Court of Appeals understood that reliance was had by the tie company upon the set-off clauses of the act is shown by its opinion, where, after sustaining the claim of the trustee that the credits in question constituted a preference, it prefaced a particular discussion of the contention, as to a right of set-off, by the following statement:

"Finally, it is said that this $2,210.73 was a credit to Harrison, and that the company should be permitted to set it off against his debt to it, and should be allowed to prove its claim for the balance remaining without restriction, on the ground that these claims were mutual debts and credits under section 68 of the bankrupt law."

The record, we think, sufficiently presented a claim of Federal right, (*Home for Incurables* v. *New York*, 187 U. S. 157,) and the objection to the jurisdiction is therefore overruled.

Passing to the merits of the controversy—

We must, at the outset, in the light of the facts found below, determine the exact relation existing between the bankrupt and the tie company, in order to fix the true import of the transactions by which the tie company, in making its claim against the bankrupt estate, asserted a right to retain and set off the sums which, in its proof of claim, it described as "deductions from pay rolls."

We think the findings establish that Harrison sold the goods, not to the tie company, but to the laborers, and therefore the result of the sale was to create an indebtedness for the price alone between Harrison and the employees. This is not only the necessary consequence of the facts stated, but likewise conclusively flows from the nature of the proof of claim made by the tie company, since that proof, so far as the items concerning the price of the goods sold to the employees are concerned, based the indebtedness by the tie company to Harrison, not upon any supposed original obligation on the part of the tie company towards Harrison to pay for the goods, but upon the "deductions from pay rolls," made by the tie company in paying its employees. The effect of this was to trace and limit the origin of the debt due by the tie company to Harrison solely to the fact that the tie company had deducted, in paying its employees, money due to Harrison by the employees which, from the fact of the deduction, the tie company had become bound to pay to Harrison. We think, also,

the facts found establish that the course of dealing between Harrison and the tie company concerning the deductions from pay rolls was that the tie company, when it made the deductions, was under an obligation to remit the money collected from the laborers for account of Harrison to him, irrespective of any debt which he might owe the tie company. This follows from the finding that, although there was a debt existing between Harrison and the tie company, the course of dealing between them was that when the tie company made deductions from the wages of the laborers of sums of money due by them to Harrison the tie company regularly remitted the proceeds of the deductions to Harrison. This conclusion, moreover, is the result of the finding that Harrison had no intention to give the tie company a preference, for if Harrison, being insolvent, to the knowledge of the company, within the prohibited period, gave to the tie company authority to collect the sums due to him by the laborers for goods sold them, with the right, or even the option, to apply the money to a prior debt due by Harrison to the company, the necessary result of the transaction would have been to create a voidable preference. And if the inevitable result of the transaction would have been to create such a preference, then the law would conclusively impute to Harrison the intention to bring about the result necessarily arising from the nature of the act which he did. (*Wilson* v. *City Bank*, 17 Wall. 486.) To give effect, therefore, to the finding that there was no intention on the part of Harrison to prefer, we must consider that the authority given by him to the tie company to collect from the laborers did not give that company the right or endow it with the option, when it had collected, to retain the money for its exclusive benefit, and to the detriment of the other creditors of Harrison.

The result of the facts found then is this: Harrison sold his goods to the laborers and agreed with the tie company that that company when it paid the laborers should deduct the amount due by the laborers from the wages which the tie company owed them, and after making the deduction should remit to Harrison the amount thus deducted, irrespective of any indebtedness otherwise due by Harrison to the tie company, Did this give rise to a voidable preference within the intendment of sections 57*g* and 60*b* of the bankrupt act?

In view of the necessary result of the findings which we have previously pointed out, it is, we think, beyond doubt that the agreement was not a voidable preference within the meaning of the statute, since, considering the agreement alone, it brought about no preference whatever. This leaves only for consideration the question whether the tie company was entitled to prove its claim, as it sought to do, for the balance owing, after crediting as a set-off the "Deductions from pay rolls," to which we have

referred. Now, as we have seen, from the facts found, it must be that the agreement between Harrison and the tie company obligated the latter, when it made the deductions from pay rolls, to remit to Harrison the amount of such deductions irrespective of the account between itself and Harrison. It follows that as to such deductions the tie company stood towards Harrison in the relation of a trustee, and, therefore, the case was not one of mutual credits and debts within the meaning of the set-off clause of the bankrupt law. (*Libby* v. *Hopkins*, 104 U. S. 303.) And, irrespective of the trust relation which the findings establish, it is equally clear from general considerations that the right to set-off did not exist. To allow the set-off under the circumstances disclosed would violate the plain intendment of the inhibition contained in clause *b* (2) of section 68 of the bankrupt act, which forbids the allowance to any debtor of a bankrupt of a set-off or counter-claim which "was purchased by or transferred to him after the filing of the petition, or within four months before such filing, with a view to such use and with knowledge or notice that such bankrupt is insolvent or had committed an act of bankruptcy." That is to say, whether or not the trust relation was engendered, the result would still be that the tie company, within the prohibited period and with knowledge of the insolvency of Harrison, acquired the claims of the latter against the laborers, with a view to using the same by way of payment or set-off, so as to obtain an advantage over the other creditors, which it was not lawfully entitled to do.

As we have concluded that under the findings there was no voidable preference, we think the court below erred in refusing to allow the tie company to prove its claim, unless it surrendered the sums which it owed Harrison and his bankrupt estate. Section 57*g* of the bankrupt act, as amended by the act of February 5, 1903, (32 Stat. 799,) empowering the court to compel creditors to surrender preferences as a prerequisite to the proof of claims against the estate of the bankrupt, relates only to those creditors "who have received preferences voidable under section sixty, subdivision *b*." But it also is demonstrated, from what we have said, that the tie company was not entitled to prove its claim as it sought to do, embracing, as it did, the assertion of a right to set-off, and thus extinguish the sum which it owed to the bankrupt estate, resulting from the deductions from pay rolls. Whilst, therefore, because of the error in imposing the condition of prerequisite surrender of the alleged preference, the judgment below was erroneous, nevetheless the court was correct in refusing to allow the alleged set-off, and in refusing to permit proof to be made which embraced and asserted such set-off. It follows that although the judgment below must be reversed for the reasons stated, the case should be remanded with directions to disregard the alleged claim of set-off, to reject any proof of claim asserting the same, and to permit a claim to be filed for the gross

indebtedness to the tie company, with the alleged set-off eliminated. The result will be that the tie company will be a creditor of the estate for the whole amount of its claim, and will be at the same time a debtor to the estate for the amount of the deductions from the pay rolls collected by it, the court below, of course, having power to take such steps as may be lawful to protect the estate in respect to the payment of dividends to the tie company, in the event that company does not discharge its obligations to the bankrupt estate.

*The decrees of both courts are reversed and the case is remanded to the District Court with directions to allow the proof of claim, rejecting the alleged set-off, and for further proceedings in conformity with this opinion.*

True copy.

Test:

*Clerk Supreme Court, U. S.*